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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

December 1, 1994

VIA HAND DELIVERY

The Honorable Reed Hundt
Chairman
Federal Communications Commission
1919 M Street, N.W.
Suite 814
Washington, D.C., 20554

Re: Ex Parte Communication
CC Docket No. 94-1 (LEC Price Caps Review)

Dear Chairman Hundt:

The undersigned parties urge the Commission to correct deficiencies in its price cap rules for Local Exchange Carriers (LECs) which will cost interstate access service customers--and, ultimately, long distance consumers--billions of dollars too much over the next four years. The productivity offset, also known as the "X" factor, currently is set at 3.3%, but should be raised to at least 5.7% consistent with the record in this proceeding. Without this increase, interstate access service rates will be $4.2 billion too high over the next four year period. We respectfully submit that the Commission must correct this deficiency as soon as possible in its ongoing review of the LEC price cap rules. Every day that passes without this correction costs consumers $3 million.

Not content with growing returns in excess of 14%, which the undersigned parties believe was generated by a too low productivity offset, LECs subject to the Commission's price cap rules have actually urged the Commission to reduce the productivity offset to 2.3%. The LECs' overreaching would result in monopoly interstate access service rates being $8.2 billion too high over the next four year period.

In addition to raising the "X" factor, the Commission should direct the price caps LECs to reduce their currently effective interstate access service rates by at least $1.3 billion. This reduction would only align LEC earnings with the 11.25% rate of return the Commission previously authorized. Unless the Commission requires such a recalibration of current rates, LEC earnings will continue to be "locked in" at 14%, even if the Commission implements a corrected "X" factor. Commission prescription of a new rate of return based on the LECs' current embedded cost of capital of roughly 10% would produce an additional reduction of $600 million.

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Raising the "X" factor to at least 5.7% and reducing interstate access service rates by $1.9 billion will cure only on a prospective basis the major existing deficiencies in the Commission's LEC price cap rules. Without these going-forward corrections, the prospects for competition in the local exchange and access service markets are dim, and without this competition our country is unlikely to realize a National Information Infrastructure (NII) which meets market needs and fuels economic growth. Commission policies which nurture and spur such competition are the best prospect for creating the NII. On the other hand, failing to correct these deficiencies and allowing the LECs to continue to earn excessive returns as a result of an incorrectly specified price cap plan would impose a multi-billion dollar dead-weight loss on our economy and jeopardize our country's telecommunications advantage in the international marketplace. None of us wants that result.

Therefore, the undersigned parties urge the Commission to correct its price cap rules by: raising the "X" factor to at least 5.7%, ordering the price cap LECs to reduce their interstate access service rates by at least $1.9 billion, retaining sharing, and renewing its commitment to competition as the right tool for building our country's NII.

Two copies of this letter have been submitted to the Commission's Secretary as required pursuant to Section 1.1206 (a)(1) of the Commission's Rules.

Sincerely,

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